

(SPACE BELOW FOR FILING STAMP ONLY)

7

WANGER JONES HELSLEY, PC
Riley C. Walter #91839
265 East River Park Circle, Ste. 310
Fresno, CA 93720
Telephone: (559) 233-4800
Facsimile: (559) 233-9330
E-mail: rwalter@wjhattorneys.com

Chapter 9 Counsel for Debtor Tulare Local Healthcare District

IN THE UNITED STATES BANKRUPTCY COURT

EASTERN DISTRICT OF CALIFORNIA

FRESNO DIVISION

In re

CASE NO. 17-13797

TULARE LOCAL HEALTHCARE
DISTRICT, dba TULARE REGIONAL
MEDICAL CENTER,

Chapter 9

DC No.: WJH-2

Debtor.

Date: Not set

Time: Not set

Tax ID #: 94-6002897

Place: 2500 Tulare Street

Address: 869 N. Cherry Street
Tulare, CA 93274

Fresno, CA 93721

Courtroom 13

Judge: Honorable René Lastreto II

**DEBTOR'S OBJECTION TO PROOF OF CLAIM NUMBER 186
IN THE AMOUNT OF \$2,370,060 FILED BY THE DEPARTMENT OF
HEALTH CARE SERVICES ON APRIL 3, 2018**

TO THE HONORABLE RENÉ LASTRETO II, UNITED STATES BANKRUPTCY
JUDGE, THE DEPARTMENT OF HEALTH CARE SERVICES, AND TO ALL OTHER
PARTIES IN INTEREST:

Pursuant to 11 U.S.C. § 502 and Rule 3007 of the Federal Rules of Bankruptcy
Procedure, the Tulare Local Healthcare District dba Tulare Regional Medical Center
(the "Debtor" or "District") objects to Proof of Claim Number 186 filed by the
Department of Health Care Services on the grounds set forth below.

JURISDICTION AND VENUE

This Court has jurisdiction to consider and determine this objection pursuant to 28 U.S.C. § 1334. This is a core proceeding under 28 U.S.C. § 157(b). Venue is proper before this Court pursuant to 28 U.S.C. §§ 1408 and 1409.

BACKGROUND FACTS

On September 30, 2017, the District filed a petition for relief under chapter 9 of title 11 of the United States Code (the "Bankruptcy Code") commencing Case No. 17-13797. Dkt. No. 1. On January 26, 2018, this Court entered the Order for Relief. Dkt. 379. On January 25, 2018, the Court approved the District's application for an order fixing the bar date for filing proofs of claim. Dkt. 366. On January 31, 2018, the District filed its proof of service of the Notice of Claims Bar Date and the "Order Fixing Bar Date for Filing Proofs of Claim" ("Bar Date Order"). Dkts. 371, 377 and 391. The Bar Date Order provided that the Claims Bar Date was April 10, 2018.

On April 3, 2018, the California Department of Health Care Services ("DHCS") filed Proof of Claim 186 in the amount of \$2,370,060 (the "Claim"). DHCS asserts that the Claim is for an overpayment of supplemental reimbursement funds under the Disproportionate Share Hospital ("DSH") program for payment year 2013/14. DHCS, as the Medicaid State Agency, administers the DSH program because it is a Medi-Cal supplemental reimbursement program. The DSH program distributes funds to hospitals that provide health care services to a disproportionately large volume of Medi-Cal beneficiaries and uninsured individuals. The District's hospital, the Tulare Regional Medical Center, was a DSH eligible hospital during the 2013/14 payment year.

As set forth in the Declaration of Jillian Mongetta ("Mongetta Declaration") submitted in support of the Claim, DHCS asserts that the District was paid \$2,370,060 in DSH funds for the 2013/14 payment year. As a recipient of DSH funds, the District is required to undergo a mandatory audit conducted by Myers & Stauffer (the "DSH Auditors"). In its Claim, DHCS also states that the former manager of the hospital operated by the District did not submit the requested data for the audit by the due date

1 of May 19, 2017, and thereafter sent a few files to the DSH Auditors but that such
2 information was incomplete and insufficient to conduct the DSH audit. The Mongetta
3 Declaration states that because the DSH Auditors did not receive the information
4 necessary to conduct the DSH audit, the District's "Uncompensated Care Costs (UCC)
5 were adjusted to zero for inpatient Fee for Service due to lack of support." The
6 Mongetta Declaration further states that since the requested data was not provided, the
7 District's "UCC were adjusted to zero for Managed Care due to lack of support." The
8 Mongetta Declaration concludes that as a result of the Uncompensated Care Costs
9 being adjusted to zero because the requested data was not provided by the District,
10 the District had a "UCC well in excess of their DSH payment" and that the District
11 "must return the entire amount of the DSH funds that they received for payment year
12 2013/14." A copy of Proof of Claim Number 186 is attached as Exhibit A to the
13 Declaration of Daniel Heckathorne ("Heckathorne Decl.").

14 After the District's former manager was terminated and Daniel Heckathorne was
15 appointed as the Interim Chief Financial Officer by the District's Board, Mr.
16 Heckathorne directed individuals working under his supervision to compile the data
17 requested by DHCS for the DSH audit for the 2013/14 payment year, and to submit
18 such data to the DSH Auditors. The requisite data was compiled, and on October 29,
19 2018, the District's representative requested that the DSH Auditors provide instructions
20 as to how that data should be transmitted to the DSH Auditors. That same day, Mike
21 Davis, a Senior Manager with the DSH Auditors, confirmed that the District had
22 provided the DSH Auditors with the required information regarding Medicare and
23 Medical payments for the 2013/14 payment year, and that it would not need additional
24 data unless the Centers for Medicare and Medicaid ("CMS") prevailed in litigation with
25 certain hospitals. Heckathorne Decl. at ¶ 4 and Exhibit B thereto. The DSH Auditors
26 have not requested that any additional data be provided. *Id.* Furthermore, on October
27 15, 2018, the DHCS sent a letter to hospital administrators which stated that the DSH
28 audit for the 2013/14 payment year were calculated based on a methodology that has

1 been determined to be invalid and unenforceable, and that DHCS had suspended its
2 effort to recoup DSH funds on that basis. *Id.* at ¶ 5 and Exhibit C thereto. For those
3 reasons, the District does not owe DHCS for any overpayment of DSH funds for the
4 2013/14 payment year asserted in the Claim.

5 **RELIEF REQUESTED**

6 By this Objection, the District requests entry of an order, pursuant to 11 U.S.C. §
7 502 of the Bankruptcy Code and Rule 3007 of the Federal Rules of Bankruptcy
8 Procedure, that provides the following relief: (a) sustains the Objection; (b) disallows the
9 Claim in its entirety; and (c) grants such other and further relief as this Court deems just
10 and proper. No previous request for the relief sought herein has been made by the
11 District to this or any other court.

12 **BASIS FOR RELIEF**

13 **A. The Legal Standard**

14 Section 502(a) of the Bankruptcy Code provides that “[a] claim or interest, proof
15 of which is filed under section 501 of this title, is deemed allowed, unless a party in
16 interest ... objects.” 11 U.S.C. § 502(a). Bankruptcy Code § 502(b)(1) states that if an
17 “objection to a claim is made, the court, after notice and a hearing, shall determine the
18 amount of such claim in lawful currency of the United States as of the date of the filing
19 of the petition, and shall allow such claim in such amount, except to the extent that ...
20 such claim is unenforceable against the debtor ... under any agreement or applicable
21 law.” 11 U.S.C. § 502(b)(1). Bankruptcy Rule 3007, which governs the procedure for
22 objections to claims, provides that “[a]n objection to an allowance of a claim shall be in
23 writing and filed.

24 **B. Burden of Proof**

25 All allegations set forth in a properly filed proof of claim are taken as true and, if
26 the allegations set forth all facts necessary to establish a claim and are not self-
27 contradictory, the proof constitutes *prima facie* evidence of the validity and amount of
28 the claim. 11 U.S.C. § 502(a); Fed. R. Bankr. P. 3001(f). However, once the objector

1 raises "facts tending to defeat the claim by probative force equal to that of the
2 allegations of the proofs of claim themselves," *Wright v. Holm (In re Holm)*, 931 F.2d
3 620, 623 (9th Cir. 1991), then "the burden reverts to the claimant to prove the validity of
4 the claim by a preponderance of the evidence." *Ashford v. Consolidated Pioneer*
5 *Mortgage (In re Consolidated Pioneer Mortgage)*, 178 B.R. 222, 226 (B.A.P. 9th Cir.
6 1995), *aff'd*, 91 F.3d 151 (9th Cir. 1996). "[T]he ultimate burden of persuasion is always
7 on the claimant." *Holm*, 931 F.2d at 623. In considering an objection to a claim, a
8 bankruptcy court may take judicial notice of the underlying records in a bankruptcy
9 case. *O'Rourke v. Seaboard Surety Co., (In re ER Fergert, Inc.)*, 887 F.2d 955, 957-
10 958 (9th Cir. 1998).

11 **C. The Objection Should Be Granted**

12 The objection should be sustained and the Claim disallowed in its entirety
13 because the District has provided evidence that the Claim should be reduced to zero
14 because it has provided all information it was required to provide to DHCS and the
15 DSH Auditors, and the DSH Auditors used a method to determine the amount of the
16 overpayment that is invalid and unenforceable.

17 As explained above, after the District's former manager was terminated and
18 Daniel Heckathorne was appointed as the Interim Chief Financial Officer by the
19 District's Board, Mr. Heckathorne directed individuals working under his supervision to
20 compile the data requested by DHCS for the DSH audit for the 2013/14 payment year,
21 and to submit such data to the DSH Auditors. The requisite data was compiled, and on
22 October 29, 2018, the District's representative requested that the DSH Auditors provide
23 instructions as to how that data should be transmitted to the DSH Auditors. That same
24 day, Mike Davis, a Senior Manager with the DSH Auditors, confirmed that the District
25 had provided the DSH Auditors with the required information regarding Medicare and
26 Medical payments for the 2013/14 payment year, and that it would not need additional
27 data unless the Centers for Medicare and Medicaid prevailed in litigation with certain
28 hospitals. Heckathorne Decl. at ¶ 4 and Exhibit B thereto. The DSH Auditors have not

1 requested that any additional data be provided. *Id.* Furthermore, on October 15, 2018,
2 the DHCS sent a letter to hospital administrators which stated that the DSH audit for
3 the 2013/14 payment year was calculated based on a methodology that has been
4 determined to be invalid and unenforceable, and that DHCS had suspended its effort to
5 recoup DSH funds on that basis. *Id.* at ¶ 5 and Exhibit C thereto. For those reasons,
6 the District does not owe DHCS for any overpayment of DSH funds for the 2013/14
7 payment year asserted in the Claim.

8 The District also objects to the Claim on legal grounds because the State of
9 California's DSH Auditors utilized and relied on FAQ responses 33 and 34 issued by
10 the Center for Medicare and Medicaid Services in conducting the DSH audit of the
11 District for payment year 2013/14, which numerous courts have determined to be
12 invalid and in violation of the Administrative Procedures Act. *Tenn. Hosp. Ass'n v. Azar*,
13 908 F.3d 1029 (6th Cir. 2018)(FAQs 33 and 34 caused DSH auditors to violate 42
14 C.F.R. §447.299(c)); *Children's Health Care v. CMS*, 900 F.3d 1022 (8th Cir.
15 2018)(FAQs 33 and 34 are not procedurally valid legislative rules and violate the
16 Administrative Procedures Act ("APA")), *Children's Hosp. of the King's Daughters, Inc.*
17 *v. Azar*, 896 F.3d 615 (4th Cir. 2018)(promulgation of FAQ 33 failed to comply with
18 APA); *New Hampshire Hosp. Ass'n v. Azar*, 887 F.3d 62 (1st Cir. 2018)(holding that
19 the rules in FAQs 33 and 34 are legislative and is procedurally improper for
20 noncompliance with the notice and comment procedures prescribed by the APA). As
21 set forth on Exhibit C to the Heckathorne Declaration, the DHCS halted its effort to
22 recoup DSH funds on that basis of one or more of those decisions in the First, Fourth,
23 Sixth and Eighth Circuit Court of Appeals. CMS withdrew FAQs 33 and 34 as of
24 December 30, 2018 in light of those four decisions. For these reasons, the District
25 believes that the DSH Audit for payment year 2013/14 by which the overpayment
26 asserted in the Claim was calculated is invalid and unenforceable, and that the District
27 does not owe any amount for the alleged overpayment of DSH funds.

1 **RESERVATION OF RIGHTS**

2 The District has not attempted to raise in this Objection each defense,
3 counterclaim, or setoff that may apply to the Claim. If a response to this Objection is
4 received, the District reserves the right to amend and supplement this Objection, or file
5 additional objections to assert any defenses, counterclaims, and/or setoffs against the
6 Claim. In all instances, the District reserves the right to file future objections or motions
7 or to supplement this Objection as to the validity, amount, or status of the Claim upon
8 different grounds than set forth herein or otherwise.

9 **CONCLUSION**

10 For the foregoing reasons, the District respectfully requests that the Court enter
11 an order granting the Objection and disallowing the Claim in its entirety.

12 Dated: July 1, 2019

WANGER JONES HELSLEY, PC

13
14 By:

Riley C. Walter

Riley C. Walter, Attorneys for Debtor
Tulare Local Healthcare District dba Tulare
Regional Medical Center